IN THE

Supreme Court of the United States

OCTOBER TERM, 1944.

No. 1205.

THOMAS M. STUBBS, As Trustee in Bankruptcy of American Bond & Share Corporation, *Petitioner*,

v.

FULTON NATIONAL BANK OF ATLANTA, *Respondent*.

On Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Fifth Circuit.

REPLY MEMORANDUM OF PETITIONER.

CLARENCE H. CALHOUN,
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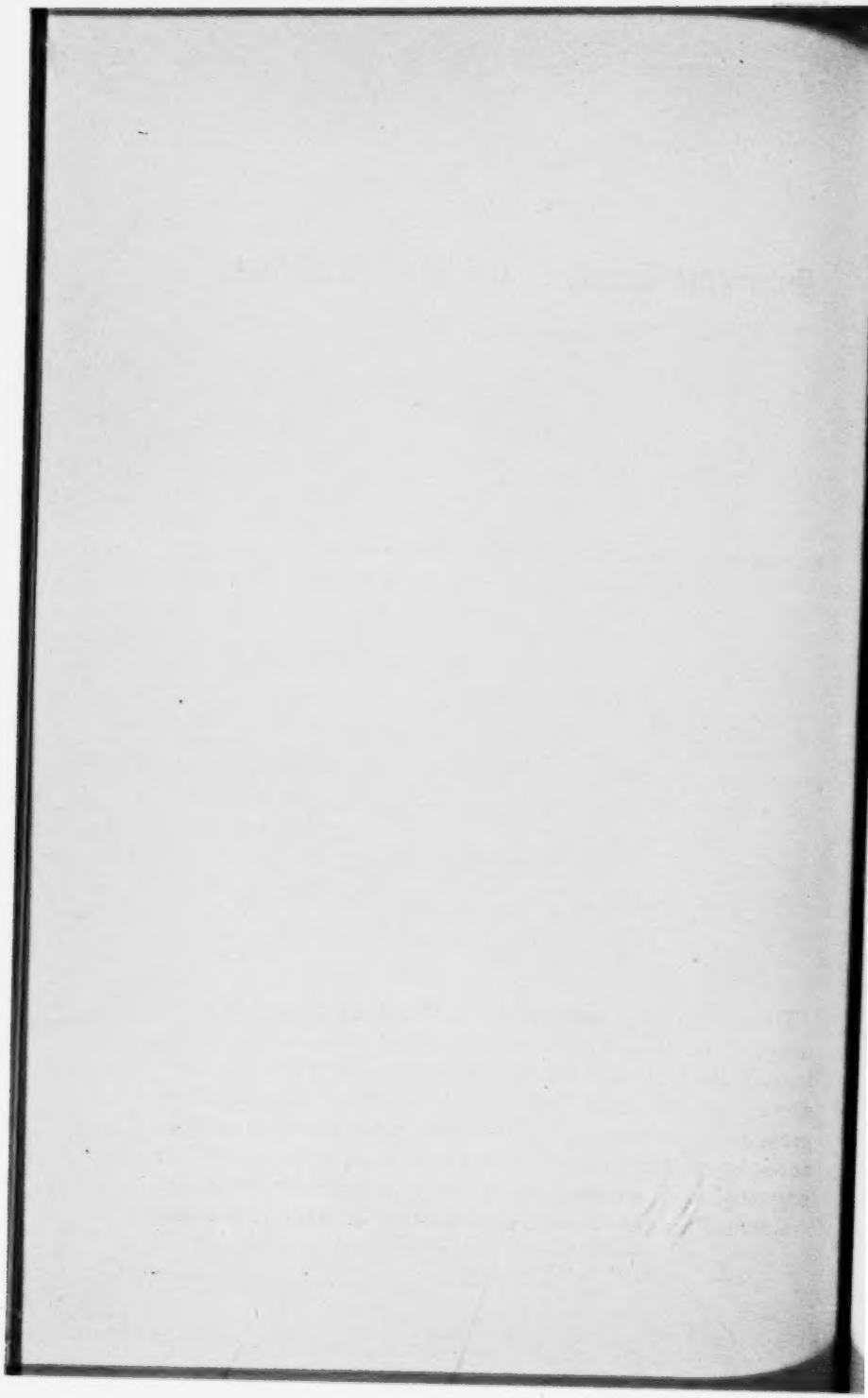

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It is significant that counsel for the Bank do not even attempt to sustain the decision of the Court below on the basis of the facts and the legal premise upon which the decision rests. The brief in opposition urges entirely different grounds of defense—grounds which were urged in and ignored by the Court below and which seem to us to have no proper place in a consideration of the petition for certiorari.

Counsel for the Bank are completely in error in the con-

tention that the consideration of the petition for certiorari by this Court would require any examination of the long record in the case. The petition was carefully drawn so as to avoid any question or ground which might conceivably require an examination of the evidence. The factual issues suggested in the brief in opposition—and a number of the facts are not correctly stated—do not relate at all to the ground upon which the decision of the Court below rests and upon which the petition for certiorari is based.[1]

The decision of the Court below rests squarely upon the legal holding—which petitioner asserts to be erroneous—that false claims by bankrupt of enormous past earnings, made by bankrupt for the purpose of deceiving customers into investing with the bankrupt, were not notice to the Bank of fraud, although the Bank had knowledge of such statements and suspected them to be false. The public importance of this holding and its conflict with the holdings of other Federal Courts are the only issues presented by the petition.

Ignoring the opinion of the Court below, the brief in opposition (pp. 6-7) assumes that the Court below could not have failed to recognize that bankrupt, in inviting investments from the public on the basis of false statements of past earnings, was guilty of fraud against its customers, making it liable to them, and likewise guilty of fraud under the Securities Act and the mail fraud statutes. It assumes also that the Court below could not have failed to recognize that the Bank, having notice that investments were being solicited upon such basis, had notice of the bankrupt's fraud on customers. Having made these assumptions, counsel for the Bank attempt to rationalize the decision of the Court below, in favor of the Bank, as holding that the particular

[1] While we would welcome a careful reading by the Court of Appendix B to the petition for certiorari, which gives a brief summary of much additional compelling evidence of notice to the Bank of fraud, no consideration of the evidence set forth in Appendix B, or of any other evidence, is necessary to a decision on the petition for the writ.

transfers here in question, while admittedly made solely for the purpose of securing funds for the carrying on of the bankrupt's business, an integral part of which was the solicitation of investments from the public upon the basis of fraudulent statements of past earnings, were not themselves tainted with the fraud inherent in bankrupt's plan of operations. The Bank apparently contends—by what odd circumstance, it does not state—that these particular transfers to it were islands of purity in a sea of fraud.

Clearly, the decision of the Court below is not based upon any such theory. The Court below did not even admit that the Bank had notice that bankrupt was defrauding its customers. The Court's position in that regard was based squarely on its erroneous view that the bankrupt's false statements of past earnings were not themselves fraudulent, but constituted legitimate "puffing." Naturally, therefore, the Court did not suggest, as counsel for the Bank would indicate, that the transfers in question were free of fraud because of isolation from the fraud on customers. There is no statement in the opinion which even tends to support Respondent's attempted rationalization of the decision below.

The suggestion in the brief in opposition that the return to bankrupt of the property transferred was relied upon by the Court below as an independent ground of defense, is entirely without justification (brief in opposition, p. 4). The Court below, having held that the Bank—because it had no notice of fraud—was not liable on the original transfers to it, held that the re-transfers of the securities to bankrupt when the loans were repaid "were not improper and invalid" (R. 983), and that the repayment to the Bank of its loans did not constitute fraudulent conveyances.[2] *Assuming the premise* upon which the Court was proceeding, that

[2] The transfers of money in repayment of the loans were charged as fraudulent conveyances in the second count of the complaint in the District Court. A consideration of that count is not involved in a consideration of the petition for certiorari.

the Bank had no notice of fraud on the part of the bankrupt, obviously the return of securities by the Bank to the bankrupt upon the repayment of the loans would create no liability upon the Bank; and the Trustee never contended otherwise. But the Court below nowhere suggests that if the original transfer constituted a fraudulent conveyance for which the Bank was liable, the Bank would have relieved itself of that liability by the return of the property to bankrupt; nor does the Court anywhere suggest, as the last paragraph of the brief in opposition would indicate, that depletion of the bankrupt's assets is a necessary element of the right to recover for a fraudulent conveyance.[3]

The decision of the Court below rests squarely upon that Court's misconception as to what, in law, constitutes fraud in securities transactions. The writ should be granted for the reasons stated in the petition.

Respectfully submitted,

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[3] While it has no proper place in a consideration of the granting of the writ here prayed, it is clear that a fraudulent transferee of property must return it to creditors without any repayment of the loan which it secures. *Cf. 1 Glenn, Fraudulent Conveyances and Preferences*, p. 529, Sec. 303. It should therefore be obvious that a fraudulent transferee, one who has notice of the transferror's intention to defraud his creditors and who thus becomes a trustee *ex maleficio* for such creditors, does not, as Bank's counsel suggest, relieve himself from this liability to account to such creditors by returning the property to the fraudulent transferror *upon repayment of his loan.*